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TAGS: ECON PGOV PREL BO
SUBJECT: IMF: ENERGY COST INCREASES DEMAND STRUCTURAL REFORM

Summary

¶1. (SBU) The annual IMF mission to Belarus terms 2007 a new economic era for the country with higher energy costs possibly knocking 5.5 percent off of GDP growth. Although the IMF notes some GOB short-term policies softened the blow, only more thorough tightening will head off the danger of the current account deteriorating sharply. Unfortunately, some GOB targets run counter to IMF recommendations. The GOB will likely use the IMF report as political cover for several unpopular policies rather than as a blueprint for wide-ranging reform. End summary.

IMF Finds GOB Must Step Up Response To Higher Energy Costs
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¶2. (SBU) In a June 4 briefing to the diplomatic corps, Balazs Horvath of the IMF's European Department said higher energy import costs imply a decrease in GDP growth of up to 5.5 percent in 2007, with additional losses each year through ¶2011. Horvath praised the move by the government to raise interest rates and partially pass increased energy costs onto consumers. However, he said wages must fall further and all cost increases (versus the current 20 percent) must be passed onto consumers to stabilize the economy.

Wide Ranging Reforms Necessary

¶3. (SBU) Horvath called for containing domestic demand through tighter macroeconomic policies that would keep the balance of payment deficit at a sustainable level. In addition to wage restraint and increases in energy prices, in the short term this includes raising interest rates and abolishing directed lending and maintaining a budgetary surplus.

¶4. (SBU) As in past years, the IMF recommended long-term structural reforms focused on ending the state's predominance in the economy. A transparent privatization should focus on increasing the competitiveness of the Belarusian economy, not on simply raising revenue. Other elements of structural reform proposed by the IMF include creating a stable business environment, lowering the tax burden by streamlining social expenditures, lowering the barriers to entry into the private sector and creating a level playing field for all investors.

GOB Appears to Pick and Choose Among Recommendations
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¶5. (SBU) Horvath told diplomats GOB end-of-year targets

contradicted the IMF's advice. For instance, while currently the budget is in surplus, the 2007 budget calls for a one and a half percent deficit, which would result in a significant and ill-advised stimulus to the economy. Similarly, the current target refinance rate of nine percent would entail a cut of two percent, whereas the IMF argues for tightening rates. On the other hand, state-controlled Belarusian Television suggested the GOB was heeding the IMF in cutting social benefits (even though the government has not yet replaced them with targeted spending, as the IMF proposes).

Comment: Those Who Take Advice Do Not Call the Shots
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¶6. (SBU) While Horvath said he saw "stirrings beneath the surface" demonstrating substantial segments of the GOB recognize the need for change, he did not attempt to counter suggestions from the diplomatic corps that the IMF report will likely fall on deaf ears. He hinted parts of the Presidential Administration did not accept his findings as completely as did other segments of the regime. Immediate reform would give Belarus the best chance at long-term economic growth. Unfortunately, Belarus will likely choose the path of least resistance by seeking loans and redirecting income from the few profitable segments of the economy to sustain loss-making enterprises whose number will likely grow along with energy costs.
Stewart